Imperial Oil Limited
and subsidiary companies

Interim report to shareholders for three months ending March 31, 1981

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The artificial island at Issungnak in the Beaufort Sea, where the company has discovered oil and gas.

Performance highlights	Three months to March 31 1980	**1981**
Financial (millions of dollars)		
Earnings	152	**146**
Revenues	1361	**1815**
Funds from operations	267	**292**
Capital and exploration expenditures	239	**227**
Operating		
Gross production		
Crude oil and natural-gas liquids (thousands of m^3/d)	36.2	**29.4**
Natural gas (millions of m^3/d)	11.3	**8.6**
Crude oil processed (thousands of m^3/d)	73.9	**70.0**
Sales		
Natural gas (millions of m^3/d)	12.1	**9.5**
Petroleum products (thousands of m^3/d)	71.6	**67.5**
Chemicals (thousands of tonnes per day)	6.0	**6.2**
Earnings per share (dollars)	1.16	**0.93**
Dividends per share (Class A) (dollars)	0.35	**0.35**

Earnings for the first quarter of 1981 were down $6 million or four percent from the corresponding period of last year. The reported earnings of $146 million include the impact of increases in the petroleum compensation charge of $20.47/m³ ($3.25 per barrel) during the quarter. This had the effect of producing a noncash gain in profits of almost $50 million (see "Inventory profits" on page 4).

The decrease in earnings from 1980 also reflects the burden placed on the natural resources segment by the National Energy Program's (NEP) new petroleum and gas revenue tax, resulting in a $24 million reduction in earnings. Declining crude production and higher operating costs continued to offset increased wellhead prices. Syncrude operated at a loss in the first quarter because of low production resulting from mechanical problems experienced late in 1980. The plant, however, was operating at close to capacity by the end of the quarter. One of the plant's units is scheduled for a routine maintenance shutdown in the second quarter.

Petroleum products earnings remained strong in the first quarter despite a six-percent reduction in sales volumes affecting all major product lines. Decreased sales are being experienced generally throughout the industry, particularly in eastern Canada. Although petrochemical earnings were slightly lower than the first quarter of 1980, performance remained strong and the outlook is encouraging.

Capital and exploration expenditures for the first three months were similar to 1980. Total investment, including increases in working capital, primarily inventory, amounted to $515 million or 176 percent of cash flow. The level of capital spending experienced last year has continued despite the reduction in cash flow resulting from the NEP. The company's plans call for continued investment in selected growth areas of its activities.

Earnings per share, based on the weighted average of 157 million shares, declined 20 percent from 1980 due mainly to the higher number of shares outstanding following the rights issue of 26 million shares in June, 1980. Dividends of 35 cents per share remained unchanged from 1980.

Consolidated statement of earnings
(unaudited)

	Three months to March 31 1980	1981
	millions of dollars	
Revenues		
Crude oil	5	119
Natural gas	61	51
Petroleum products	1054	1341
Chemicals	187	205
Investment income and other operating revenue	54	99
	1361	1815
Expenses		
Exploration	67	41
Purchases of crude oil and products	596	903
Operating	162	231
Marketing and administration	129	145
Interest	16	12
Depreciation and amortization	39	51
Commodity, property, and other taxes	80	102
Petroleum and gas revenue tax	–	24
	1089	1509
Earnings before income taxes	272	306
Income taxes	120	160
Earnings for the period	152	146

Consolidated statement of changes in financial position
(unaudited)

	1980	1981
Funds (a) were provided from		
Operations (b)	267	292
Proceeds from sales of property, plant, and equipment	2	1
	269	293
Funds were used for		
Dividends	46	55
Reduction of long-term debt	6	7
	52	62
Funds remaining for reinvestment	217	231
Investment		
Capital and exploration expenditures	239	227
Increase in working capital other than funds	96	288
	335	515
Deficiency of funds before financing	118	284
Financing		
Capital leases	–	5
Long-term debt	–	–
Capital stock	4	2
	4	7
Decrease in funds	114	277

Approved by the board

Armstrong
Chairman and chief executive officer

J G Livingstone
President

Operating statistics

	Three months to March 31 1980	1981
Exploration and development		
Gross exploratory wells drilled		
Oil	–	2
Gas	29	18
Dry	15	4
Gross development wells drilled		
Oil	15	3
Gas	11	4
Dry	4	2
Gross production		
Crude oil		
Conventional and natural-gas liquids (thousands of m^3/d)	34.2	27.0
Syncrude (thousands of m^3/d)	1.1	1.5
Cold Lake (thousands of m^3/d)	0.9	0.9
	36.2	29.4
Natural gas (millions of m^3/d)	11.3	8.6
Refining		
Crude oil processed at company refineries (thousands of m^3/d)	73.9	70.0
Refinery capacity utilization at March 31 (percent)	97	91
Sales		
Petroleum products (thousands of m^3/d)		
Gasolines	24.3	23.4
Middle distillates	28.3	25.6
Heavy fuel oils	5.9	5.9
Lubricants, greases, specialty oils, and other	13.1	12.6
	71.6	67.5
Natural gas (millions of m^3/d)	12.1	9.5
Chemicals (thousands of tonnes per day)		
Petrochemicals	2.5	3.0
Fertilizer	1.6	1.7
Building materials	1.9	1.5
	6.0	6.2

Shareholder information
(unaudited)

	1980	1981
Average number of Class A and B shares outstanding, weighted monthly (thousands)	130 695	156 943
Share prices (Class A) (dollars)		
High	57½	36⅜
Low	36½	30⅝
Close at March 31	41⅝	33⅛
Dividends paid (millions of dollars)	46	55
Dividends per share (dollars)	0.35	0.35
Earnings per share (dollars)	1.16	0.93
Funds from operations per share (dollars)	2.04	1.86

Notes to the financial statements

(a) Funds represent cash, marketable securities, and short-term loan, less short-term notes.

(b) Funds from operations comprise earnings before exploration expenses, adjusted for depreciation, deferred income taxes, and other items not affecting funds.

Activities of particular interest

Imperial accused of "rip-offs"

The company has vigorously denied allegations of unethical business conduct made in a report by the Bureau of Competition Policy of the federal department of consumer and corporate affairs on *The State of Competition in the Canadian Petroleum Industry.* The report accused major integrated Canadian petroleum companies, including Imperial Oil, of having engaged in predatory and restrictive practices and other "monopolistic" activities between 1958 and 1973. Despite these accusations, no charges have been laid.

At a press conference in Toronto on March 6, Chairman and Chief Executive Officer J. A. Armstrong emphasized that Imperial Oil obeys both the letter and intent of the law and cited evidence of competitive forces at work in the Canadian petroleum industry.

The report will form the basis for an inquiry under the Combines Investigation Act, which is expected to begin in the autumn of 1981. Imperial has stated that it welcomes the opportunity of replying to the allegations made against it and that an impartial inquiry will find no evidence of wrongdoing by the company.

Norman Wells expansion

The company has applied for approval to build facilities to increase production of crude oil and natural-gas liquids from 500 m^3/d to 4800 m^3/d at the Norman Wells field in the Northwest Territories.

After extensive public hearings, a federal Environmental Assessment Review Panel recommended some additional studies in a report published in January, 1981. The company will complete these studies in 1981.

In April, the National Energy Board approved an application by Interprovincial Pipe Line (NW) Ltd. for a pipeline connecting Norman Wells to the southern pipeline network. Cabinet approval is needed before construction of the line can start.

Western provinces exploration

The company participated in 18 successful gas wells and two successful oil wells in the western provinces during the first three months of 1981.

Activity continued but at a significantly reduced rate in the Elmworth area where five successful gas wells were completed in association with Canadian Hunter Exploration Ltd. and Sulpetro Limited.

Arctic exploration

As the first quarter ended, the company was drilling a follow-up well to the Issungnak discovery made in the Beaufort Sea in 1980. This well, in which the company has a 50-percent interest, will assess the potential of deeper formations and further evaluate a number of zones in which oil, gas, or both were either tested or indicated. Results are expected during the second quarter.

In the Arctic islands, the company participated with the Arctic Islands Exploration Group in a significant oil and gas discovery at Skate, an offshore well 18 km northeast of Lougheed Island. It also participated in two gas discovery wells, one at Cisco, 26 km northeast of the Whitefish gas discovery drilled in 1979, and the second at MacLean, 27 km east of Lougheed Island. All of these wells are located on ice islands.

During the first quarter of 1981, the Arctic Islands Exploration Group completed its commitments to earn an interest of 60 percent in lands held by Suncor Inc. The group expects to complete its commitments to earn the same interest on lands held by Global Arctic Islands Limited during the second quarter of 1981.

The company has an interest of 35 percent in the Arctic Islands Exploration Group.

Inventory profits

The federal government's National Energy Program assesses a petroleum compensation charge on crude oil delivered to refiners. This charge in turn is reflected in the price of product sold to customers. Under the company's accounting practice, inventory is valued by the first-in, first-out (FIFO) method, which is also allowed for income-tax purposes. Old inventory costs are therefore matched with current sales under FIFO, creating an "inventory profit," however these profits must be reinvested in inventories, the value of which now includes the petroleum compensation charge. The "inventory profit" for the first quarter was almost $50 million.

There is actually a net cash reduction to the company since income taxes are payable on the "inventory profits." The cash drain is approximately 45 cents for every $1 of compensation assessed.

Replacements for Alberta crude cutbacks

Reductions in the supply of light Canadian crude oil arising from cutbacks in Alberta production are being absorbed by Montreal refiners. On the basis of historical crude runs in Quebec, Imperial's share of the reduction is 17 percent. It is expected to be replaced with foreign crude oil and refined products. These were readily obtainable in the first quarter of 1981 due to decreased world demand. The higher costs should be offset by the federal government's special compensation program.

Although heavy Canadian crudes are available from Saskatchewan, their increased residual fuel production and higher sulfur content preclude running them in significant volumes through Ontario and Montreal refineries.

The cutbacks began on March 1 and reduced the company's production of conventional crude oil by eight percent or 2050 m^3/d.

Coal operations

Early in 1981, the company acquired all outstanding shares of Byron Creek Collieries Limited, with the approval of the federal government. Last year, the mine produced 900 000 tonnes of thermal coal. The company is considering an expansion of production to 3.6 million tonnes by 1985 if sufficient reserves are found and sales contracts secured.

The company also holds an interest of six percent in Quintette Coal Limited and has the right to earn up to 16.75 percent. Quintette reports it has signed a basic agreement with Japanese interests to buy at least the first 15 years' proposed production of metallurgical coal. Proposed annual production is five million tonnes of metallurgical coal and one million tonnes of bituminous thermal coal.

New fertilizer plant started

Construction began during the first quarter on a $400-million plant to produce nitrogenous fertilizer, following approval by the Alberta cabinet. The plant will be located beside the company's existing agricultural-chemicals complex at Redwater, Alta. About 200 construction workers are employed at the site; their number is expected to increase to 700 by autumn. The plant is scheduled for completion in 1983.

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